Summary of Testimony of Martin McBroom, Director Federal Environmental Affairs, American Electric Power before the House Subcommittee on Energy and Environment

American Electric Power (AEP) is one of our nation's largest electricity producers. AEP utilizes a diverse generating fleet – coal, nuclear, hydroelectric, gas, oil and wind – to serve over five million retail consumers in 11 states. But of particular note, AEP is one of the largest coal-fired electricity generators in the U.S. We are committed to working with you to pass federal legislation that is well thought-out, achievable, and reasonable. A well-designed federal regulatory program will allow AEP and others to obtain recovery of costs for the commercialization and deployment of advanced technology to reduce greenhouse gas emissions. We believe legislation can be crafted that does not impede AEP's ability to provide reliable, reasonably priced electricity to support the economic well-being of our customers, and includes mechanisms that foster international participation and avoid creating inequities and competitive distortions that could otherwise harm the U.S. economy. AEP is one of the first companies to publicly endorse actual cap-and-trade legislation, as introduced in Congress, to reduce greenhouse gas emissions across the U.S. economy.

AEP and the International Brotherhood of Electrical Workers (IBEW) urge Congress to include in federal climate change legislation a provision to encourage rapidly developing countries to also curb their greenhouse gas emissions, and to thereby ameliorate very real trade distortions arising from a failure to develop a climate initiative comparable to that of the United States. During the last session of Congress, the IBEW-AEP proposal was included in several climate bills in the Senate and the House, including Chairman Markey's bill (H.R. 6186, Title VII Subtitle G), for which we and our partners are grateful. This proposal is also supported by the International Brotherhood of Boilermakers, Iron Ship Builders, Blacksmiths, Forgers and Helpers; and the United Mineworkers of America. We believe any international strategy must prevent the undue shifting of U.S. jobs to countries – such as China and India – which have yet to take comprehensive steps to limit their greenhouse gas emissions. This is of concern to AEP because 38% of our electricity generation serves industrial customers who could be directly impacted if this provision is not included. In addition, any greenhouse gas reductions that our nation makes in isolation will be overwhelmed and rendered moot by huge and rapidly increasing emissions coming from fast-growing, developing countries. Unless emissions from rapidly developing nations are addressed, we would face the worst of both worlds, namely unchecked rampant growth in greenhouse gas emissions from those nations and the loss of American jobs and industries.

The IBEW-AEP proposal seeks to address the impacts discussed above by requiring that importers submit international reserve allowances sufficient to cover the emissions attributable to greenhouse gas intensive goods they are importing into the United States. Notably, this allowance requirement would only apply to imports from countries opting to <u>not</u> take "comparable action" to limit their emissions, as compared to the effect of actions taken in the U.S. Failure to submit such allowances would bar entry of covered goods into the U.S. This allowance requirement has been designed for compatibility with World Trade Organization (WTO) rulings. International reserve allowances would be derived from a pool that is entirely separate from the allowances provided under the domestic cap-and-trade program. This would assure that the demand for, and use of, international reserve allowances cannot disrupt the availability, price or use of domestic allowances. The allowance requirement has also been designed to maximize effectiveness in limiting greenhouse gas emissions by focusing on imports with the greatest carbon footprint -- goods whose greenhouse gas emissions can be quantified and tracked with reasonable accuracy and administrative ease.

The international allowance requirement would only apply as a measure of last resort. The U.S. would first make good-faith efforts to persuade other countries to limit their greenhouse gas emissions. WTO jurisprudence under the GATT exception for conservation measures suggests that if America negotiates with one affected party, as our nation almost certainly will, then the U.S. must negotiate with all parties directly affected by the provision. These negotiations would begin during the time required to promulgate domestic regulations, and conclude before the domestic cap takes hold. International negotiations would not delay application of the international provision. Consistent with WTO jurisprudence, America would inform any affected nations of a clear and knowable standard for application in the near future. Notably, the U.S. is not required under WTO jurisprudence to delay application of the allowance requirement on imports for a specific length of time after the start of the domestic cap-and-trade program. The IBEW, AEP and those who share our view believe that nations could be notified of the standard, and the international provision applied, at about the same time as the domestic cap takes effect. Finally, the proposal provides U.S. climate negotiators with essential leverage they will need to convince major emitting nations to participate, and to assure the American people of the fundamental fairness and symmetry of the Herculean task we face. Global political pressure for action on climate change is growing. That momentum, and the need for all major emitting nations to reduce their own domestic emissions -- when coupled with the leverage provided by the IBEW-AEP proposal – strongly suggests that this proposal may never actually have to be implemented. However, it provides the assurance of an essential backstop that America and its hardworking businesses and families must have.

TESTIMONY OF
MARTIN McBROOM,
DIRECTOR, FEDERAL ENVIRONMENTAL AFFAIRS,
AMERICAN ELECTRIC POWER
BEFORE THE
U.S. HOUSE ENERGY AND COMMERCE
SUBCOMMITTEE ON ENERGY AND ENVIRONMENT
March 18, 2009

Good morning Mr. Chairman and distinguished members of the Subcommittee on Energy and Environment of the House Committee on Energy and Commerce.

Thank you, Chairman Markey, for this opportunity to offer the views of American Electric Power (AEP) on how the United States can effectively engage developing countries to help ensure that they too limit their greenhouse gas emissions. Ensuring that these nations take actions that are comparable to our own is essential to achieving a global solution to the most important environmental and energy challenge facing the United States and indeed, the world.

My name is Martin McBroom. I am the Director for Federal Environmental Affairs of American Electric Power (AEP). Headquartered in Columbus, Ohio, AEP is one of the nation's largest electricity generators -- with over 36,000 megawatts of generating capacity -- and serves more than five million retail consumers in 11 states in the Midwest and South Central regions of our nation. AEP's generating fleet draws upon a wide array of fuel sources – including coal, nuclear, hydroelectric, natural gas, oil – and wind energy to meet our customers' needs. Furthermore, coal plays a prominent role in our fuel portfolio. AEP uses more coal than any other electricity generator in the western hemisphere. AEP recognizes coal must continue to play an important role for providing reliable and affordable electricity to our customers, and indeed, virtually all Americans and an increasing share of the world's population. In recognition of these realities, we are working to perfect new advanced coal technologies that capture or otherwise reduce CO_2 emissions from our generating fleet.

Over the past decade, AEP has voluntarily implemented a broad portfolio of actions to reduce, avoid or offset greenhouse gas emissions. In addition, we continue to invest in new clean coal technology plants and R&D initiatives that will enable AEP, our industry and the world to meet the challenge of significantly reducing greenhouse gas emissions over the long term. For example, AEP is designing and is committed to building a highly-efficient new generating plant using the most advanced technology in Arkansas (e.g., ultra-supercritical coal combustion) and has also launched several projects to demonstrate our ability to capture and store CO_2 from coal-fired power plants.

AEP Support for Federal Climate Legislation

We are committed to working with you to pass federal legislation that is well thought-out, achievable, and reasonable. A well-designed federal regulatory program will allow AEP to obtain recovery of costs for the commercialization and deployment of advanced technology to reduce greenhouse gas emissions. We believe legislation can be crafted that does not impede AEP's and others' obligation to provide reliable and reasonably priced electricity to further the economic well-being of our customers. Furthermore, we believe that such legislation also must include mechanisms that foster international participation and avoid creating inequities and competitive distortions that would otherwise harm the U.S. economy.

AEP is proud to have been one of the earliest companies to publicly endorse actual cap-and-trade legislation, as introduced in Congress, to reduce greenhouse gas emissions across the U.S. economy. AEP supports reasonable legislation, and is not calling for an indefinite delay until advanced technologies, such as carbon capture and storage (CCS) technologies, are developed. However, as the requirements become more stringent and we move beyond the ability of current technology to deliver those reductions, it is essential that requirements for those very substantial reductions coincide with the commercialization of advanced technology.

Need for Global Solution

AEP, just like many others, is heartened by your strong interest in including in federal climate change legislation a credible provision to encourage rapidly developing countries to also curb their greenhouse gas emissions. This is an issue that has profound ramifications for our global environment, and equally huge consequences for our national economy. These dynamics inspired

Mr. Edwin D. Hill, International President of the International Brotherhood of Electrical Workers (IBEW), and Michael G. Morris, Chairman, CEO and President of AEP, to collaboratively develop what we believe to be an essential ingredient and an effective policy response to the international ramifications arising from unilateral federal climate change legislation. Our joint legislative proposal focuses on the regulation of imported goods to induce foreign governments to take effective action to limit their countries' greenhouse gas emissions. Notably, our proposal – the key details of which I will discuss later – was included in all of the economy-wide cap-and-trade bills that were introduced during the last session of Congress. It was included in the Lieberman-Warner, Boxer Substitute, and Bingaman-Specter in the Senate. It also, Mr. Chairman, was not only included in your bill (H.R. 6186, section 101, which would create Title VII Subtitle G of the Clean Air Act), but also the Doggett bill and Dingell-Boucher discussion draft in the House. Thank you for doing this.

There is strong support for the proposal among labor unions. In addition to the IBEW, the proposal is supported by the International Brotherhood of Boilermakers, Iron Ship Builders, Blacksmiths, Forgers and Helpers; and the United Mineworkers of America.

The need for a global solution to climate change should be apparent to all. While the United States must clearly do its share, any greenhouse gas reductions that we make in isolation will be overtaken – literally swallowed up – by the huge and rapidly increasing emissions coming from the fast-growing, developing countries. Let me offer a few facts that demonstrate this point:

- The International Energy Agency (IEA) projects world-wide energy-related CO_2 emissions will increase by 57 percent between 2005 and 2030, with developing countries driving more than three-quarters of this CO_2 growth.

- China and India alone are expected to account for 56 percent of the worldwide increase in CO_2 emissions during the 2005-2030 timeframe.

- China's CO_2 emissions are growing faster than any other country. Recent reports suggest that China is now the world's number one emitter of CO_2 annually.[1]

[1] CRS Report for Congress, *China-U.S. Relations: Current Issues and Implications for U.S. Policy*, at page 25 (December 21, 2007).

- China's coal use as a percentage of world consumption increased from about 20 percent in 1985 to over 29 percent in 2003. By 2025 it will likely be consuming almost 40% of the world's coal.

- Coal accounts for at least two-thirds of China's current energy consumption, with demand exceeding 2 billion tons of coal per a year. By way of comparison, this is nearly twice the present demand for coal in the United States. [2]

- China's appetite for fossil fuels has resulted from the rapid growth of its energy-intensive industries. China Steel, for example, has increased its share of the global steel production from 13 percent in 1996, to 35 percent in 2005. As a result, China is now by far the world's largest steel producer, making more steel than the next six producers (Japan, the United States, Russia, Korea, Germany, and Ukraine) combined.

- Other energy-intensive industries in China also have experienced rapid growth in recent years. As a result, China now makes about one-half of the global production of cement and flat glass, and about one-third of worldwide aluminum production. In the case of aluminum, an industry report indicates that China has built the equivalent total aluminum capacity of the U.S. and Great Britain combined in only three years.

- Much of China's rapid industrial growth is fueled by electricity generated by new coal-fired power plants. In 2006 alone, for example, China brought into service 90,000 megawatts of new coal-fired generating capacity – which amounts to two large coal-fired generating units per week. Notably, this also is equivalent to about one-third of the total U.S. coal-fired capacity in operation today.

- China's greenhouse gas emissions are rapidly increasing with this strong growth in coal use, combined with very robust economic growth. Emissions have increased by 80 percent since

[2] These figures are likely to be overly conservative estimates in light of a recent New York Times article that reports: "Last year, China burned the energy equivalent of 2.7 billion tons of coal, three-quarters of what experts had said would be the maximum required in 2020. To put it another way, China now seems likely to need as much energy in 2010 as it thought it would need in 2020 under the most pessimistic assumptions." New York Times, *As China Roars, Pollution Reaches Deadly Extremes* (December 26, 2007).

1990 and are projected to rise by another 65 percent by 2020.

The magnitude of these emissions trends only underscores the need for action by the United States, in concert with China, India and the other fast-growing developing countries. A failure to effectively ensure that these developing countries also do their part would mean that even if the United States imposes a stringent emissions cap on our entire economy, this cap will accomplish very little to reduce global greenhouse gases. We have come to recognize that regardless of the strength and achievement of any domestic reduction program Congress may craft – unless coupled with effective international measures to ensure rapidly developing nations also promptly address this problem – no one will succeed at curbing global loadings of greenhouse gases. If Congress does not also effectively address emissions from fast-growing developing nations, it would be inadvertently encouraging the shift of economic activity from the United States to other countries precisely because they would not be doing their part in reducing greenhouse emissions. Furthermore, unless a viable mechanism is established to ensure that our friends in fast-growing developing nations join us, there can be no assurance of a net global reduction in greenhouse gas emissions. Such reductions are widely recognized to be necessary to adequately address the risks of climate change. Thus, we have come to see that such a provision is essential to America's and the world's success in tackling global warming.

Linkage of Trade and Climate

Viewed in this context, it is apparent that trade is an important key to developing effective federal climate change policy. The United States cannot develop an effective domestic greenhouse gas reduction program unless we also create a parallel federal policy to address the potential impact that uncapped greenhouse gas emissions in fast-growing developing countries would have on U.S. trade and competitiveness in a world economy. This clear linkage between climate and trade requires that we combine our domestic reduction program with an effective, defensible, international strategy. That international strategy must ensure that fast-growing developing countries take concrete steps to limit their overall greenhouse gas emissions, and thus, prevent the undue shifting of U.S. jobs to those same countries. If the production of currently-produced, carbon-intensive products shifts from the U.S. to countries utilizing less-efficient power production technology, this greatly exacerbates the effect upon the environment.

That production shift is of concern to AEP because 38% of our electricity generation serves industrial customers who would be potentially impacted if this provision is not included in final enacted legislation. When factories close and move overseas, AEP loses industrial customers, and our residential customers, who work in those facilities, lose their jobs and their families are hard hit as a result.

Put in its simplest terms, U.S. climate legislation must be linked with a world-wide effort to reduce greenhouse gas emissions, and thus keep America's jobs and economy on an equal footing with other major-emitting nations. To do less would result in the worst of both worlds, namely the failure to avert major adverse impacts from global climate change and the loss of American jobs and manufacturing industries to uncapped nations.

The IBEW and AEP have proposed a credible approach for addressing these concerns arising from a stringent domestic reduction program. In developing this, we have strived to establish regulatory mechanisms that would not jeopardize U.S. competitiveness and American jobs, relative to developing nations. In addition, we have worked hard to craft those mechanisms in a manner that complies with the Agreement Establishing the World Trade Organization (WTO). Specifically, we respectfully recommend that you require that allowances accompany energy-intensive imported goods from rapidly developing countries if they do not promptly take comparable action to limit their own greenhouse gas emissions.

Core Elements of IBEW-AEP Proposal

The IBEW-AEP proposal seeks to equalize the adverse impacts discussed above by requiring that importers submit international reserve allowances to cover emissions attributable to certain greenhouse gas intensive goods they are importing. Failure to tender such allowances would bar entry of such covered goods into the United States. We have designed this allowance requirement for WTO consistency. We also have designed the allowance requirement to maximize its effectiveness in limiting greenhouse gas emissions and not affecting U.S. competitiveness by focusing on imports with the greatest carbon footprint.

First, the allowance requirement is narrowly focused on greenhouse gas-intensive goods, such as iron, steel, aluminum, cement, glass, paper and other such products whose greenhouse gas

emission can be quantified and tracked with reasonable accuracy and administrative ease. In the event that this range of goods is not sufficient to impact the behavior of a particular nation, our proposal provides authority to expand the range of goods as may be necessary and administratively feasible.

Second, the allowance requirement only applies to imports from those countries that have not taken "comparable action" to limit their greenhouse gas emissions, as compared to the emissions reductions achieved in the United States. Comparable action may include cap-and-trade programs or other measures that foreign countries may implement to achieve greenhouse gas reductions and which are recognized to be comparable in effect to the levels achieved here. As discussed below, our proposal establishes specific criteria for evaluating actions undertaken in each country and in determining, on a case-by-case basis, whether the country has taken comparable action. In addition, our proposal focuses only on those countries that contribute significantly to global emissions and would not burden the poorest developing countries with low emissions or low standards of living. This corresponds to a long standing principle that has guided U.S. international climate negotiations through a bipartisan succession of administrations. Namely, we suggest that least developed countries that suffer from widespread poverty and low levels of emissions should not be required to take such actions. This also comports with WTO rules explicitly recognizing the least developed countries as a unique category. The allowance requirement therefore does not apply to imports from least developed nations and those countries whose greenhouse gas emissions are below a *de minimis* percentage of total global emissions.

We believe that determinations, such as which nations are not taking comparable action and, if not, how the allowance requirement is calculated for each sector in those nations, are best left to an independent U.S. government agency. For these reasons, our proposal recommends establishment of an independent commission that is charged specifically to carry out these and other essential functions under the program.

And third, the allowance requirement would only apply as a measure of last resort. This ensures consistency with WTO rulings. Notably, our proposal contemplates that the United States would first make good faith efforts to persuade other countries to limit their greenhouse gas emissions. Only if these efforts fail with a particular foreign country would the commission be authorized to apply the allowance requirement to covered goods imported from that non-participating

country. WTO jurisprudence under the GATT exception for conservation measures suggests that if we negotiate with one affected party, as we almost certainly would, then we must negotiate with all parties directly affected by the provision. These negotiations can begin once the legislation is enacted, and continue during the intervening time period that is necessary to write domestic regulations, and conclude before the emissions cap is placed on U.S. industry. The negotiations therefore would not cause any delay regarding the application of the international provision, which is recommended to occur two years after the beginning of the domestic cap.

The IBEW, AEP and our allies hope that the allowance requirement – if adopted – would never actually be applied to U.S.-bound exports from fast-growing developing countries. Our proposal provides U.S. climate negotiators with considerable leverage that they can draw upon to encourage comparable action by developing countries. In fact, the use of the IBEW-AEP proposal as an effective means to prompt international action has already been demonstrated by the previous administration while in Bali, Indonesia. This suggests that as a measure of last resort – requiring allowances for imports – may never actually have to be applied to any country.

Another key aspect of our proposal is the timeframe for implementation. In addition to providing sufficient time for international negotiations, as just described, our proposal requires the United States to take several other steps before imposing allowance requirement on imports. Most importantly, the U.S. must determine that a country is not taking "comparable action" to limit its greenhouse gas emissions.[3] This determination would require an independent commission to quantify the annual emissions reductions that the U.S. has actually achieved under its domestic program, and assess whether that country has achieved a percentage change in its greenhouse gas emissions that is the same as or better than the percentage change achieved domestically. Countries that meet the test are automatically recognized to have taken comparable action and would therefore be excluded from the international allowance program. For nations not yet excluded, the commission is authorized to exclude those countries that are taking comparable action based on the extent to which a nation has deployed state of the art technology in major sectors of its economy and implemented regulatory programs or measures for limiting greenhouse gas emissions. In assessing whether, and to the extent that, other countries are taking comparable action, the commission cannot

[3] As already noted, a comparability determination need not be performed for certain countries that are otherwise excluded from the allowance requirement. These excluded countries include least developed nations and those countries whose greenhouse gas emissions are below a specified *de minimis* percentage of total global emissions.

focus on the precise form of the country's measures to limit its greenhouse gas emissions, but rather, upon the reductions actually achieved by those measures.

The allowance requirement for imports from those countries that fail to take comparable action would be applied two years after the start of the U.S. program. Immediately upon enactment, the President would notify all foreign countries of the caps and the negotiating objective to secure commitments from major emitters to take comparable action. These countries would then be on notice that should they fail to take comparable action, their exports to the U.S. would eventually have to be accompanied by offsetting international reserve allowances. At the end of the first year of the U.S. domestic program, the United States would measure the results of our cap-and-trade program and other measures implemented in the U.S., and show that we have done what we claimed we would do. During the second year, once the results are known, the independent commission would determine which countries had taken comparable actions based on comparability criteria described above. At the start of the third year, the U.S. would begin to impose the allowance requirement on imports from those countries that fail to take comparable action to limit their greenhouse gas emissions.

Following this sequence, even under a tight timetable, would ensure WTO compliance. The key point, based on WTO jurisprudence, is that the commission must inform the affected nations of a clear and knowable standard that would then be applied in the near future.

This proposal cannot be dismissed as "protectionist." In this example, the allowance requirement on imports would not actually be applied to any country outside of the United States until about five or six years after the enactment of domestic cap-and-trade legislation. The Congress appears unlikely to pass such legislation until late 2009 or sometime in 2010 at the earliest, suggesting that the international provision would not be applied until 2015 or 2016. The date of implementation of the IBEW-AEP provision upon the exports to the United States from a foreign nation depends on the date of enactment of U.S. climate legislation, and how long it takes to promulgate regulations for the entire domestic program. Such an extended timeframe rebuts erroneous suggestions that the intent of a U.S. international allowance requirement would be to protect U.S. industry, particularly given that protectionist trade measures generally take effect almost immediately.

There have been suggestions that this implementation timetable should be moved further out, and that more years should be allowed, in light of the likely grant of allowances to competitive industry. This proposal should be considered with great care, in light of the evolution of the proposal, and concern for American workers.

The IBEW-AEP provision, as originally introduced in a number of bills (including Chairman Markey's bill, H.R. 6186), contemplated that the international allowance requirement would be applied in 2020 against nations that fail to take comparable action. If you assume that a climate bill is enacted in 2009 or 2010, and it takes at least three years to write regulations, this meant that there would be a six- or seven-year gap between the actual application of a cap in the U.S. as compared with the application of the allowance requirement against the good imported from a non-participating foreign nation. There has been a strong concern across industry and unions alike that this would compel jobs and factories to leave the U.S. during the interval from when a cap starts, until the international allowance requirement and comparability standard would become active. This concern was expressed before the idea of giving substantial amounts of free allowances to industries impacted by competition was under active consideration.

To address this concern, the start date of the border allowance requirement was moved up in the Doggett bill and Dingell discussion draft, and the Boxer Manager's Amendment in the Senate, so that it applies two or three years after the application of the domestic cap. As explained above, this shorter time frame is both WTO compliant as well as administratively feasible. This change was made in those bills that included a very generous grant of allowances to U.S. industries. The rationale was that those industries should not be adversely impacted by a brief delay when they are receiving allowances, and that a two- or three-year delay is more practical in terms of administrative application.

Whether even more time should be allowed -- more than two years -- is in the capable hands of this Committee to determine. Some of the industries who sharply argued that a six- or seven-year gap is unacceptable are represented here today, so you may wish to pose the question to them. Do those industries believe that their concerns regarding competitiveness during that period will be addressed by allowances, so that more time can be allowed before the IBEW-AEP provision were to be implemented? Those same industries sharply criticized the delay of six or seven years, so our counsel to the Committee is to determine, in advance and before free allowances would be disbursed

to those industries or before changing the date of the application of the IBEW-AEP allowance requirement, whether the industries believe that their competitiveness is secured by free allowances. If they believe they are not, it both suggests that free allowances alone are not sufficient, and that the IBEW-AEP provision is absolutely vital to ensure that developing countries act effectively to reduce their own greenhouse gas emissions, and thereby address the underlying competitiveness concerns.

Even if industry responds in the affirmative, since industry receives the financial benefit of the allowances, the Committee should consult with trade unions and carefully evaluate the consequences of doing so. As noted in the discussion below on free allowances, we recommend that the Committee not set the implementation date at 2020 in the next legislative vehicle unless sufficient safeguards have been included to absolutely guarantee that the allowances are used to keep jobs in the United States. Nor should it be accepted at face value that the date needs to be set as late as 2020. Rather, the focus should be on the development of a well-coordinated package that includes the IBEW-AEP proposal to generate leverage in international negotiations and that uses free allowances to safeguard American workers and guarantees that jobs stay here at home. That is a key question before you set the start date of the import allowance requirement, and recreate the date gap that was the policy rationale for moving up the start date in other legislation.

Relationship to the Domestic Program

Another important aspect of our proposal is that it would work in conjunction with, and would not detract from, the domestic cap-and-trade program it mirrors. Importers would comply with the allowance requirement by purchasing "international reserve allowances" from the U.S. government. The international reserve allowances would be drawn from a pool that is entirely separate from the allowances provided under the domestic cap-and-trade program. This would assure that the demand for, and use of, international reserve allowances for imports under the international program cannot distort the availability, price or use of allowances within the domestic program. Similarly, this separate allowance allocation cannot breach the U.S. emissions cap or otherwise undermine the environmental goals of the domestic program. Importantly, international reserve allowances would never be used to comply with the domestic cap-and-trade program. Rather, importers could only use them for meeting their allowance-holding requirements that apply to imported covered goods, in the

event that an exporting country's government elects to not do its part to reduce greenhouse gas emissions.

To ensure WTO compliance, we recommend a parallel emission trading mechanism for importers which emulates the one established for the domestic program. International reserve allowances, for example, may be traded or banked for future use. Importers would also have alternative compliance options that would be identical to those provided to regulated entities under the domestic program. This flexibility would allow importers to achieve compliance by obtaining – in lieu of international reserve allowances – either foreign allowances that are issued pursuant to another country's cap-and-trade program or emissions offsets from domestic or international projects that meet certain minimum criteria. Finally, the price of the international reserve allowances would be pegged at the U.S. price for domestic allowances. This approach is recommended to further assure close correlation between the cost of compliance under the international and domestic programs.

Finally, the IBEW-AEP provision is expressly designed to complement and work in conjunction with an allocation of allowances or auction revenues to industries that are impacted by competitive pressures, should Congress decide to grant such an allocation. The complementary nature of the two is confirmed by the direct leverage that our proposal can have on large developing countries to take comparable action, and would be an indispensable tool that would assist our negotiators. By contrast, the primary benefit of granting free allowances goes to U.S. manufacturers. Specifically, the free allowances help to minimize the adverse international competitive impacts and thereby prevent U.S. production (and the associated greenhouse gas emissions) from moving offshore to uncapped countries. However, when combined, the two provisions safeguard U.S. manufacturers in a WTO-consistent fashion and provide leverage for prompting comparable action by all of the rapidly developing nations.

The IBEW-AEP provision is also complementary because it would accomplish critically important policy objectives that we believe cannot be addressed by granting free allowances to U.S. manufacturers alone. First and foremost, the IBEW-AEP provision is an indispensable tool for use by our negotiators to convince fast-growing developing countries to take comparable action, and would assist U.S. negotiators to achieve a truly global solution, while making sure it is not accomplished at the expense of American workers. By contrast, the granting of free allowances to U.S. companies would simply have no impact on the behavior of any large emitting nation – none at

all. We believe that America needs a credible, WTO-compliant backstop, and that is why we respectfully recommend that you include the IBEW-AEP provision, as Chairman Markey did last year in H.R. 6186.

Second, allowances are a valuable resource and, as a result, Congress may decide to phase out any free allocation over time. Further, as reflected in the Obama Administration Budget proposal, there will be strong political pressure to auction the allowances. The resulting auction revenues may well be used to fund "big ticket" federal initiatives such as tax cuts or health care so that there would be little left to assist industries impacted by competition. Manufacturers will need the help of both free allowances and the impact abroad of the IBEW-AEP provision – and for that reason Congress should use both given the ephemeral nature of free allowances or auction revenues. The IBEW-AEP provision, and its impact on regulation of greenhouse gas emissions abroad, would provide an essential backstop, should free allowances be phased out under an auction, or if auction revenues are consumed by other budgetary priorities.

Third, the IBEW-AEP provision helps equalize the playing field by requiring comparable action from large emitting developing countries. Persuading that country to regulate its greenhouse gas emissions is primarily aimed at the achievement of the overall goal of U.S. climate change legislation. In addition, American workers will benefit. By contrast, it will be difficult to design an iron-clad system that can guarantee that the cash benefits of allowances will in fact be used to place American jobs on an even footing. The Committee should ensure that the companies are not receiving even more allowances than they actually need for this purpose, and that it is carefully targeted by sector and even individual factory, since not all sectors or factories are equally impacted. (An output-based approach solves part of this problem, since cash rebates or free allowances are based on current output of manufacturing plants. However, an output-based approach may still not solve all problems, since such rebates might still not have a strong, absolute and documented relationship to trade competition, and this problem is only magnified at the sector level.)

This is a complex undertaking, and if not carefully designed, could fail to stop manufacturers from moving their operations overseas. The IBEW-AEP provision, by contrast, indisputably helps achieve U.S. objectives under all future implementation scenarios. It does so by treating greenhouse-gas intensive goods from rapidly-developing nations in a fashion comparable to our own goods. This is a fundamentally fair premise, and no more or less than you are asking of the American people

themselves. As noted above, we support both approaches, because when combined, the two provisions safeguard U.S. manufacturers in a WTO-consistent fashion and provide leverage for prompting comparable action by all of the rapidly developing nations.

Fourth, the international negotiations for the next post-Kyoto treaty are a huge and complex undertaking that operates by consensus. These negotiations will ultimately only be successful if all of the world's nations sign and ratify the resulting treaty. If the U.S. is unable to negotiate an international agreement that requires all countries – including the developing world's large emitters – to achieve comparable greenhouse gas reductions, then the IBEW-AEP provision would become a critically important backstop to protect the environment and to ensure American workers are not disadvantaged.

On the other hand, if the next treaty does include such commitments, then large emitting nations will meet the standard of comparability within the IBEW-AEP provision. Some argue that developing countries would prefer that this form of leverage not be available to U.S. negotiators, and they worry that allusions to protests by developing country officials about the IBEW-AEP provision are a problem. We disagree. The Committee should consider complaints by large developing country emitters about the IBEW-AEP proposal to be strong evidence that the proposal will serve the Congress precisely as it is intended – as an effective tool with which to induce those countries to take action to control their greenhouse gas emissions.

In summary, the IBEW-AEP approach is designed to also work with a grant of free allowances to U.S. industry impacted by trade competition, should the Congress decide to grant such an allocation. A well designed allocation of allowances, with tough safeguards, should ensure that the monetary benefits of those allowances are used to keep jobs at home and directly help American workers. The IBEW-AEP provision and a grant of allowances, working together, would have a strongly positive effect upon American workers. But this symbiotic approach is critical, and this dual approach is essential. Granting allowances or auction revenues alone would not be sufficient to safeguard U.S. workers and manufacturers impacted by trade competition from the largest emitting nations in the developing world.

WTO Compliance

As noted throughout this testimony, we have sought to design a program that complies with WTO law. We have carefully crafted a parallel allowance system for imports that is intended to:

- Avoid discrimination between countries where the same conditions prevail; and
- Maintain rough comparability in the burden on imported and domestic allowances.

Although the particulars of WTO law are beyond the scope of this testimony, we believe that the United States would be in a strong position to defend our program if it were subject to a WTO challenge by another country. Furthermore, the proposal provides the independent commission and the EPA Administrator with authority to adjust the international program to ensure consistency with WTO obligations.

Detailed supporting material for AEP's view on WTO compliance is attached as an appendix to this testimony. Generally speaking, the attached legal analysis explains the grounds for WTO compliance based on the fact that the allowance requirement for imports is consistent with each of the following WTO criteria:

- The allowance requirement is directly linked to the environmental objective of addressing global climate change by reducing otherwise unfettered greenhouse gas emissions attributable to imports from other countries, in a fashion closely similar to what the U.S. will itself implement.

- If you accept our recommendation, it would establish a flexible measure for imports that is adaptable to and respectful of the circumstances of each exporting country, and therefore devoid of arbitrary or unjustifiable discrimination. Each exporting country would have our much-preferred choice of implementing credible greenhouse gas emission reduction program as an alternative to compelling importers into acquiring and presenting allowance certificates, and our trading partners would be given a predictable standard in advance with which to achieve compliance.

The design, architecture, and structure of such an international allowances requirement would demonstrate that the system has no purpose other than to cause the reduction of greenhouse gas emissions and does not operate as a trade barrier or as a protectionist measure.

Concluding Remarks

AEP strongly supports your efforts to enact into law federal climate change legislation. This legislation should establish reasonably achievable targets and timetables for reducing greenhouse gas emissions on an economy-wide basis. An essential element of the legislation is an international provision that also requires fast-growing, developing countries to take comparable actions to those of the United States. This would provide an essential backstop to ensure that our domestic initiatives to address the environmental risks of climate change are not negated by rampant growth of greenhouse gas emissions elsewhere in the world.

Inclusion of such an international provision is essential to ensure the passage of mandatory federal climate change legislation. The Senate famously signaled its objections to unilateral U.S. action to cap domestic emissions with its unanimous passage of the Byrd-Hagel resolution. That resolution stated that no treaty mandating greenhouse gas reduction commitments for developed countries should be ratified unless it also "mandates new commitments to limit or reduce greenhouse gas emissions for Developing Country Parties within the same compliance period." Given that the Congress is now considering concrete actions to limit U.S. greenhouse gas emissions prior to the ratification of such a treaty, it is paramount that the federal legislation contain an effective provision for encouraging fast-growing developing countries to also comparably curb their greenhouse gas emissions. We believe that the most effective way to achieve this objective and to address the underlying policy concerns raised in the Byrd-Hagel resolution is by imposing an allowance requirement on imports from non-participating nations, which incorporates the essential thrust of the IBEW-AEP proposal, and respects WTO jurisprudence.

Mr. Chairman, AEP hopes that these suggestions will be helpful to you and your Committee colleagues in developing a solution for engaging developing countries to actually join with America in meeting the climate challenge. Thank you again for this important opportunity to testify.

Summary of WTO Analysis

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Summary of WTO Consistency of the IBEW — AEP Proposal

The IBEW-AEP proposal ("proposal") is **legal under WTO** because it applies to imports of carbon-intensive products the same types of environmental measures as the United States would apply within the United States under a cap-and-trade program. Indeed, the proposal **explicitly requires** that the requirements on imports be adjusted to ensure **consistency with international agreements** (e.g., section 101 of Chairman Markey's bill (110th Congress, H.R. 6186), which would create section 766(b)(2) of the Clean Air Act).

The proposal **hits the mark set by WTO case law** under either the GATT national treatment obligation or the GATT exception for measures relating to the conservation of exhaustible natural resources.

The ultimate goal of the proposal is that the proposed import measures never take effect – that the leverage offered to U.S. negotiators equipped with the credible threat of WTO-compliant measures will induce large emitters to take effective action promptly on their own and through international negotiations to limit GHG emissions.

To serve that goal, the proposal meets **all applicable WTO requirements** of the exception for environmental measures, including:

(1) securing a **close "ends-means" relationship** with the overall environmental objectives of the cap-and-trade program;
(2) implementing measures **in conjunction with limitations on US production,** in an **"even-handed"** fashion so that foreign goods are not treated worse than domestic goods;
(3) adjusting import requirements to **take into account different conditions among countries**;
(4) allowing time for **good faith negotiating efforts** with **all** affected countries; and
(5) allowing time to **measure U.S. emissions reductions** before imposing trade measures.

Each of these elements is discussed below:

(1) The proposal provides a real solution to the conservation objective of reducing greenhouse gas ("GHG") emissions.

- GATT Article XX(g) provides a general exception to the GATT's substantive obligations only for those government measures that are "primarily aimed at" the conservation of exhaustible natural resources.
- In *US – Shrimp*, the WTO Appellate Body recognized that a government measure was primarily aimed at the conservation of an exhaustible natural resource

because "a close and genuine relationship of ends and means" existed between the measure and the conservation objective.

- Under the current proposal, importers could meet the requirements by providing allowances from recognized cap-and-trade programs outside the United States, or by securing international reserve allowances from the U.S. Government.

- **In contrast, a carbon tax on imports would have no direct relationship to the reduction of emissions abroad.**

(2) The proposal, which would place restrictions on the importation of certain foreign products, is implemented in parallel with restrictions on domestic production.

- GATT Article XX(g) applies "if such measures are made effective in conjunction with restrictions on domestic production or consumption" -- language that the WTO Appellate Body has interpreted as requiring "even-handedness."

- In other words, as explained by the Appellate Body in *US – Gasoline*, restrictions on imported products must be "promulgated or brought into effect together with restrictions on domestic production or consumption of natural resources."

- However, the Appellate Body also made clear in *US – Gasoline* that GATT Article XX(g) does not require "identical treatment of domestic and imported products."

(3) The proposal is structured so as to take into consideration the different conditions that may exist in affected exporting countries.

- According to the Appellate Body in *US – Shrimp*, the *chapeau* of GATT Article XX requires that a government measure "be designed in such a manner that there is sufficient flexibility to take into account the specific conditions prevailing in any exporting Member."

- **In contrast, a single carbon-intensity standard for all products in a particular sector could not meet this requirement.**

- In *US – Shrimp*, the Appellate Body found unacceptable government measures that "require other [WTO] Members to adopt essentially the same comprehensive regulatory program, to achieve a certain policy goal, as that in force within that Member's territory, without taking into consideration different conditions which may occur in the territories of those other Members."

- Moreover, the Appellate Body has found a government measure that "condition[s] market access on the adoption of a programme comparable in effectiveness" (versus the same program) satisfies the *chapeau*'s requirements because the measure permits sufficient flexibility in its application.

(4) The proposal provides sufficient time for the U.S. Government to engage in serious negotiations with all affected countries to curb GHG emissions before the international allowance requirement would enter into effect.

- The Appellate Body rejected the government measure at issue in *US – Shrimp* in part because of "[t]he failure of the United States to engage the appellees, as well as other Members exporting shrimp to the United States, in serious, across-the-board negotiations with the objective of concluding bilateral or multilateral agreements for the protection and conservation of sea turtles, before enforcing the import prohibition against the shrimp exports of those other Members."

- Moreover, in *US – Shrimp*, the Appellate Body found a violation of the anti-abuse provisions in the *chapeau* because "the United States negotiated seriously with some, but not with other Members" that were similarly situated.

- To be clear, the Appellate Body has not interpreted GATT Article XX to require that WTO Member government negotiate with other governments before it imposes an environmental measure is imposed. Rather, the *chapeau* of GATT Article XX requires non-discrimination, so that if a WTO Member government chooses to negotiate with some countries, it must negotiate with all countries that would be affected by a measure.

    - The United States is already negotiating climate issues with other nations, and the United States will discuss the application of the international allowance provision with some of the nations that are affected by it. To meet the GATT Article XX criteria, therefore, the United States will be obligated to negotiate with all of the countries to which the provision will be applied (but not those exempted from the measure), because the United States will be negotiating with some of them.

- The United States is not required to conclude negotiations – only to make serious, good-faith efforts with all (approximately thirty) affected countries. The negotiations could commence immediately upon passage of the legislation and enactment into law. Thus, the requirement to negotiate does not affect the date on which the allowance requirement would be imposed on imports from affected countries.

(5) The proposal imposes the international allowance requirement on imports at about the same time as the application of the cap-and-trade requirements to domestic production, and importers will be provided in advance the standard of comparability of action.

- In US – *Tuna I*, the GATT 1947 Panel noted (in an unadopted report) that because the United States had "linked the maximum incidental dolphin-taking rate which Mexico had to meet during a particular period in order to be able to export tuna to the United States to the taking rate actually recorded for United States fisherman during the same period," the "Mexican authorities could not know whether, at a given point of time, their conservation policies conformed to the United States conservation standards." The Panel concluded that "a limitation on trade based on such unpredictable conditions could not be regarded as being primarily aimed at the conservation of dolphins."

- As proposed, the allowance requirement would be applied on imports after the U.S. Government measured emissions reduction in the United States and provided that standard of "comparability" to producers in and importers from affected countries. Under WTO jurisprudence, the United States must apply the measure to affected countries in an "even-handed" manner as compared to the manner in which it is applied to U.S. production or consumption. If the United States requires concrete verification and measurable results in exporting countries, it will be difficult for the United States to justify not doing so with respect to the results achieved domestically under the cap.

- On the other hand, if the United States were to apply the allowance requirement on imports without any measurement or verified results of GHG emissions reductions inside the United States, then "even-handedness" would appear to require the United States to treat affected foreign countries in a similar fashion – without any measurement or verification of GHG emissions abroad.

WTO Background Analysis

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WTO Background Analysis of International Provisions of U.S. Climate Change Legislation

The United States Congress is contemplating legislation that would impose a mandatory cap-and-trade program for U.S. greenhouse gas (GHG) emissions. This legislation must also provide leverage to ensure that emissions in other countries, particularly rapidly developing countries such as China or India, do not undermine these efforts to protect the environment. To provide effective leverage, the U.S. legislation must be compliant with the Agreement Establishing the World Trade Organization (WTO). To that end, the International Brotherhood of Electrical Workers (IBEW) and American Electric Power (AEP) have proposed that the United States impose an allowance requirement on imports of carbon-intensive goods from countries that fail to take action on GHG emissions comparable to that of the United States.[1] The proposal was reflected in section 101 of Chairman Markey's bill (110th Congress, H.R. 6186), which would amend the Clean Air Act and create Title VII Subtitle G ("Global Effort to Reduce Greenhouse Gas Emissions"). The proposal was also reflected in Title XIII Subtitle A of S. 3036, the Manager's Substitute Amendment to the Lieberman-Warner bill, which was considered but not voted upon by the United States Senate in June 2008.[2] Counsel for AEP has prepared the following legal analysis on the WTO-consistency of such a requirement.

I. Summary

Where governments take action to address environmental protection, WTO law favors doing so through consensual and multilateral procedures, rather than unilateral trade measures. However:

- if the United States made **good faith efforts** to negotiate with **all affected** nations on a non-discriminatory basis but was unable to reach agreement on procedures to reduce greenhouse gas emissions, then

- the United States could **require imports** of goods to be accompanied (electronically) by emissions **allowances**,

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[1] A summary of the IBEW-AEP proposal is attached.

[2] Senate Amendment 4825, 110th Congress, *reprinted at* Cong. Rec. S5049, S5091-S5095 (June 4, 2008) (hereinafter "Manager's Amendment").

- in the context of a broader requirement that **domestic producers** have emission allowances.

Analyzing the WTO-consistency of an allowance requirement on imports is a two-step process: (1) is the requirement, as a measure, **consistent** with the relevant obligations of the WTO, and if not; (2) is it covered by a WTO **exception**?

One could argue that an allowance requirement on imports should be considered as part of the overall U.S. cap-and-trade program. As such, it would be consistent with the WTO national treatment obligation set forth in GATT Article III:4, because it would be administered to accord imported goods treatment no less favorable than the treatment accorded "like" domestic goods. If the allowance requirement on imports were not considered as part of domestic regulation, then it would be governed by the obligations set forth in GATT Article XI or II regarding border measures. Exempting goods from least developed countries, and countries with less than a *de minimis* amount of GHG emissions, from the allowance requirement would likely violate GATT Article I:1, requiring non-discriminatory ("most-favored-nation") treatment among foreign trading partners. Even if the measure were not consistent with applicable WTO obligations, however, the allowance requirement would be covered by the WTO exception set forth in GATT Article XX(g) for measures relating to the conservation of exhaustible natural resources or the exception set forth in GATT Article XX(b) for measures relating to the protection of human, animal or plant life or health. The allowance requirement, under which allowances submitted with imports would be retired from further use, just as allowances assigned to domestic production would be, is closely related to the conservation objective of the overall climate change program. It is also an important part of a comprehensive regulatory scheme that is apt to cause substantial benefits to health and life.

The relevant WTO provisions are included in an Appendix attached to this memorandum, and the following chart illustrates the results of the WTO analysis:

WTO ANALYSIS	**ALLOWANCE REQUIREMENT ON IMPORTS**
1. Is measure consistent with WTO obligations?	
(a) Issue	**Either** it is considered as part of internal regulation . . .
- Applicable provisions	GATT Article III
- Outcome	WTO consistent if judged in the context of overall domestic regulation, affords national treatment, *i.e.,* treatment to imported goods no less favorable than that accorded to "like" domestic goods.
(b) Issue	**. . . or** it is judged as a border measure.
- Applicable provision	GATT Articles II and XI
- Outcome	Not WTO-consistent if the measure imposes charges in excess of scheduled duties or border restrictions.
(c) Issue	Does it discriminate among goods from different countries?
- Applicable provision	GATT Article I

- Outcome	Not WTO consistent if the measure exempts least developing countries or countries with *de minimis* emissions
2. If the measures is not WTO consistent, then is it covered by a WTO exception . . .	
(a) Issue	**Either** measure relates to the conservation of exhaustible natural resources . . .
- Applicable provision	GATT Article XX(g)
- Outcome	Yes, it is closely related to the objective of conservation
(b) Issue	**. . . or** measure is necessary to the protection of human, animal or plant life or health . . .
- Applicable provision	GATT Article XX(b)
- Outcome	Yes, even though in the short term it may be difficult to isolate the contribution of a single measure to reducing climate change, it is part of a comprehensive regulatory scheme that is apt to induce sustainable change.
3. . . . and the "chapeau" to Article XX?	Is the measure applied in a manner that does not arbitrarily or unjustifiably discriminate between countries where the same conditions prevail, or is not a disguised restriction on trade?
- Applicable provision	Article XX chapeau
- Outcome	Yes, focusing on top emitting countries, and only those that had not addressed GHG emissions, would be justified because of clear link to GHG emission reduction goals; the measure is flexible and not "capricious" or "random" and the rationale for discrimination relates to the policy objective.
4. Result?	**YES, MEASURE IS PERMISSIBLE UNDER WTO RULES**

II. Description of Measure

The domestic context for GHG-related trade measures would be a **cap-and-trade program** under which the U.S. Government would determine a **quantitative cap** for GHG emissions, and establish quantitative **emission allowances,** the sum of which would equal the U.S. GHG emissions cap. This system would be modeled on the EPA's existing U.S. cap-and-trade program in its Acid Rain Program,[3] with some differences. The government would issue electronic allowance certificates (each with a unique serial number for tracking and safeguards against counterfeiting) to show the amount of GHG emissions allowed. The certificates could then be transferred or sold in an **allowances market**. A firm emitting more GHGs than its existing allowances would permit would need to procure additional allowances or would be penalized for exceeding its allowances. All firms generating GHGs would have to continually monitor and report their emissions.

[3] Described at http://pubweb.epa.gov/air/clearskies/captrade.html, last visited January 25, 2008.

A domestic cap-and-trade program, implemented without measures to address GHG emissions from outside the United States, would be ineffectual in addressing the full range of GHG emissions affecting the environment. An allowance requirement imposed on imports would help to secure the environmental benefits of the overall program.

Under the IBEW-AEP proposal, the U.S. Government would **negotiate** with GHG emitting countries to secure internationally agreed disciplines on GHG emissions. Before and after U.S. implementing regulations were promulgated, the U.S. Government would begin to measure on an annual basis the reduction of GHG emissions in sectors under the U.S. cap and use those data to determine whether and to what extent key sectors in other countries had taken comparable action. The determination would be based, therefore, on the impact on GHG emissions rather than the precise form of the regulatory program used to achieve those effects. The U.S. Government would focus its determination on those countries that contribute most to global GHG emissions – least developed countries and countries with less than a *de minimis* volume of GHG emissions would be excluded.

If the U.S. Government determined that a country did not take comparable action, then an importer of certain goods from that country would be required to provide allowances to the U.S. Government corresponding to the GHGs emitted when the imported goods were produced in the country of origin. The U.S. Government would use an **adjustment factor** in setting the number of allowances required for imported goods. This adjustment factor would reflect the portion of allowances that domestic producers receive at no cost in relation to the allowances that domestic producers procure by auction. The adjustment factor would also reflect the conditions prevailing in different countries.

Which imported goods would be subject to the requirement? The scope of imported goods subject to the allowances requirement could be set to match as nearly as possible the scope of the domestic requirement. Thus, if the requirement were to apply only to the production of **carbon-intensive goods**, or only to “upstream” rather than “downstream” products, then the scope of imports covered by the requirement could be set accordingly. This contributes to ensuring non-discriminatory treatment of imports. It should be noted, however, that the purpose of a domestic cap-and-trade program is to introduce a price of carbon into the entire economy, regardless of which entities were subject to domestic allowance requirements. Accordingly, the scope of the imported goods subject to the allowances might be set more broadly.

What would be the source of these certificates? Under one approach, importers would secure allowances from the normal supply of allowances made available for U.S. entities to satisfy their obligations under the U.S. cap-and-trade system. Thus, importers could obtain U.S. emissions allowances from the producer/exporter or brokers operating generally in the marketplace. Alternatively, the U.S. Government could establish a separate (unlimited) supply of allowances that would only be used by importers. Finally, the U.S. Government could **permit importers to satisfy their obligations using allowances (and credits) generated under the cap-and-trade systems of other countries**. The Bingaman-Specter and Lieberman-Warner bills introduced in the 110th Congress combined the last two approaches.

III. Is the Measure Compliant with U.S. International Obligations?

In order to effectively persuade major newly industrializing economies to participate in GHG reduction, U.S. legislation must be permissible under WTO rules.[4] Two key principles of WTO law are germane to assessing the WTO legality of measures that could be used as part of a cap-and-trade program:

- each WTO Member government must obey its market access commitments on import tariffs, and cannot otherwise block imports (GATT Articles II, XI);

- it also may not use its domestic taxes, or **any** domestic regulations, so as to discriminate in favor of domestic goods compared to like imported products, or in favor of imported goods from one foreign country rather than another (GATT Articles I, III).

In accordance with these principles, the legal status of a measure under the GATT may be different depending on whether it is a border measure or whether it is an internal measure enforced at the border. GATT Article II:1(b) prohibits new import charges, and Article XI:1 prohibits bans or quantitative restrictions on imports. A measure that comes under either GATT article would likely be WTO-inconsistent. However, under GATT Article III, a WTO Member is entitled to regulate all products that are sold in its market provided that internal regulation does not afford protection to domestic over imported goods.

Thus, notwithstanding the prohibitions embedded in Articles XI:1 and II:1(b), a restrictive internal regulation (such as a residue limitation or product ban) or a prohibitive internal excise tax can be enforced on imports at the border, and be judged under GATT Article III, rather than Articles XI or II. In other words, the border-enforced internal measure would be completely GATT-consistent as long as it is non-discriminatory. The Note to Article III shows how the GATT draws the line between border measures and border-enforced internal measures. The Note identifies two issues that must be considered: does the tax, charge or regulatory requirement apply **both** to an imported product and to the like domestic product, and is it collected or enforced "at the time or point of importation"? The stated policy purpose of a measure is not relevant, nor is its categorization by domestic law.[5]

The following analysis examines whether the allowance requirement on imports is consistent with the WTO market access commitments and non-discrimination obligations for trade in goods. GATT law considers the regulation of imported goods either as a border measure, or as part of an overall program of internal regulation, but not both. There are good arguments that the allowance requirement is best understood as part of internal regulation, but it is a very close question. We review both sets of arguments below.

[4] We focus here only on WTO rules, as the WTO Agreement is the only agreement that binds both the United States and major countries of concern to Congress. Other U.S. treaties would also apply to climate change legislation, but the basic principles would not differ.

[5] *EC – Regulation on Imports of Parts and Components*, GATT BISD 35S/37 (1990), paras. 5.6-5.7.

A. Consistency with WTO Market Access Commitments

To simplify this analysis, we consider an allowance requirement as it applies to a hypothetical ton of steel produced and exported from Country X and a "like" ton of steel (*i.e.*, same physical characteristics and uses) produced in the United States. Of course, actual trading patterns may be more complex, involving multi-stage processing across borders, and some imported products are not produced in the United States.

As stated above, Articles II:1(b) and XI:1 are the GATT provisions that are relevant in assessing whether an allowance requirement on imports is a border measure, and as such, whether it is consistent with the WTO **market access** commitments of the United States. First, GATT Article II:1(b) prohibits the imposition of any new extra charges or surcharges on products that are subject to tariff concessions—and close to 100 percent of U.S. imports are now under such concessions. If the allowance requirement program mandated that only importers—as opposed to importers and domestic producers—buy allowance certificates or pay an extra charge, it would constitute a new border charge, and as such, it would violate GATT Article II:1(b). Second, GATT Article XI:1 prohibits any border measure restricting imports other than duties, taxes or other charges. By requiring that importers present allowance certificates as a condition for importation, the allowance requirement program could cause a decrease in the volume of imports. As a result, the program would constitute a border measure that imposes a quantitative limitation on imports in violation of GATT Article XI:1.

If the allowance requirement on imports is a border measure under either GATT Article II or Article XI, it will not be consistent with the WTO market access commitments of the United States. To have a chance of surviving WTO scrutiny at this first level of analysis, the allowance requirement must be justifiable as an internal measure that falls in line with the WTO non-discrimination obligations of the United States.

B. Consistency with WTO Non-Discrimination Obligations

GATT Article III is the most important provision, for the purposes of this analysis, embodying the non-discrimination principle of the WTO.

In contrast to the interpretation described above, the United States could argue that the allowances requirement should be considered an internal regulation subject to the national treatment obligation set forth in GATT Article III:4. To ensure compliance with Article III:4, the United States could adjust the scope of imported goods covered by the allowances requirement, and the number of allowances required to be submitted for particular imported goods. A WTO dispute settlement panel might point out, however, that the allowances program is a regulation on U.S. **producers**, whereas, the allowances requirement on imports is a regulation on imported **products**. On that basis, the Note to Article III might rule out classifying the allowances requirement on imports as an internal regulation subject to Article III.[6] But the United States could respond that the scope of

[6] The distinction between a regulation of U.S. *producers* and a regulation of imported *products* is based on the product-process doctrine. Under the doctrine, the line is not drawn between regulations of products on the one hand and regulations of producers and production processes on the other. Rather, it is drawn between regulations of products and regulations of producers and production processes that affect characteristics of the product on the one hand, and regulations of producers and production processes that do **not** affect characteristics of a product on the other. See Robert

Article III has been interpreted more flexibly than a hard-and-fast, line-drawing exercise would permit. For example, a measure, such as this one, regulating whether and how products, including domestic products, can be sold constitutes an internal regulation for purposes of Article III.

As an internal regulation, the allowance requirement on imports would be subject to GATT Article III:4, under which the United States must accord to imported products "treatment no less favourable than that accorded to like products of national origin in respect of all laws, regulations and requirements affecting their internal sale, offering for sale, purchase, transportation, distribution or use." A note to Article III provides that "[a]ny internal tax or other internal charge, or any law, regulation or requirement . . . which applies to an imported product and to the like domestic product and is collected or enforced in the case of the imported product at the time or point of importation, is nevertheless to be regarded as an internal tax or other internal charge, or a law, regulation or requirement . . . and is accordingly subject to the provisions of Article III."[7] When an internal tax (such as VAT or an excise tax) is collected on imports at the border, that is called a *border tax adjustment*.

These provisions mean that if the U.S. imposes a regulation (such as the EPA's rules on gasoline composition under the Clean Air Act), the regulation must treat imported products no less favorably than like U.S. products. The internal U.S. measure can be enforced on imports at the border, but it must not discriminate against imports. In determining whether a measure discriminates against imports, WTO panels look to its effect on the conditions of competition between the domestic product and imported like products.[8]

Finally, there are two more non-discrimination requirements in the GATT that would be relevant. The most-favored nation (MFN) clause in GATT Article I:1 prohibits discrimination between foreign sources of supply. The MFN clause applies to border charges of any kind, to internal taxes or regulations, and to border enforcement of internal taxes or regulations. Under Article I:1, whenever a WTO Member grants an advantage, favor, privilege or immunity to a product from any country, it must accord that advantage, favor, privilege or immunity to the like product of any WTO Member. In addition, GATT Article XIII requires non-discriminatory application of any quantitative restrictions on imports.

If all imported steel from any foreign country were equally subject to the allowances program and received equal treatment, then the measure would be consistent with Article I:1. If an imported ton of steel from Country X were subject to the allowances measure but a "like" ton of steel from Country Y were not (for example because Country Y has a different set of arrangements with the U.S. to meet the objectives of GHG emission reduction), then it would raise questions under GATT Article I:1. However, the United States could argue that, under GATT Article I:1, it is entitled to impose conditions on the importation of products, provided that those conditions apply in the same way to imported

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Hudec, *The Product-Process Doctrine in GATT/WTO Jurisprudence* in M. Bronckers and R. Quick, *eds*., NEW DIRECTIONS IN INTERNATIONAL ECONOMIC LAW,187, 191-92.

[7] GATT, Note *Ad* Article III. The "*Ad* Notes" to the GATT have coequal status with the main GATT text.

[8] The focus on "conditions of competition" is a consistent theme in cases applying GATT Article III since 1957; as one example, *see Korea – Measures Affecting Imports of Fresh, Chilled and Frozen Beef* ("*Korea – Beef*"), WT/DS161/AB/R, WT/DS169/AB/R, 11 December 2000, at para. 135, finding that treatment no less favorable under Article III "means…according *conditions of competition* no less favourable to the imported product than to the like domestic product."

products from all sources.[9] The United States could exclude from the allowance requirement of imports from WTO Members whose GHG emissions are below a *de minimis* threshold, which would capture most of the WTO Members that are considered by the United Nations to be least-developed countries.[10] With respect to the largest GHG emitting countries, the United States might point out that the climate change-related objective is the same, but the treatment of Country X and Country Y steel differs because the objective is being met in different ways. The Appellate Body might consider this argument under GATT Article I:1, just as it has in cases applying GATT Article III:4.[11] However, this would be a novel argument in relation to Article I:1, and textual differences between Articles I and III would need to be taken into account in applying this argument to Article I.

IV. Applicability of WTO Exceptions

This portion of the analysis focuses on whether any of the general WTO exceptions for trade in goods would permit the United States to maintain the allowance requirement on imports.

Even if a government measure would ordinarily conflict with the market access and non-discrimination provisions of the GATT, the violation may be excused by one of the ten special policy-based exceptions provided in GATT Article XX. These exceptions apply when a measure is taken for particular purposes or under particular circumstances listed in Article XX. To prevent abuse, these exceptions are all subject to two safeguards provided in a general opening clause ("*chapeau*") to Article XX. The WTO Appellate Body has developed a standard "two-tiered" method for applying Article XX: first, examine whether a measure falls within one of these policy-based exceptions; second, determine whether it complies with the anti-abuse safeguards in the *chapeau*.[12] The following analysis concentrates on paragraph (g) of Article XX, which has been used in similar situations. Paragraph (b) of Article XX, covering measures "necessary to protect human, animal or plant life or health," could also apply to the measures described above. The "necessary" condition under paragraph (b) has been interpreted strictly in WTO jurisprudence although the Appellate Body has recently suggested that it should provide additional flexibilities when the measure is part of a comprehensive regulatory scheme or where there is a long-lead time between implementation and the expected result.[13]

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[9] Panel Report, *Canada – Certain Measures Affecting the Automotive Industry*, WT/DS139/R, WT/DS142/R, adopted 19 June 2000, modified by Appellate Body Report, WT/DS139/AB/R, WT/DS142/AB/R, DSR 2000:VII, 3043, paras. 10.23-10.24.

[10] Described at http://www.unctad.org/Templates/Page.asp?intItemID=3618&lang=1, last visited January 25, 2008.

[11] For instance, in one case, the WTO Appellate Body found that the detrimental effect of a measure on imports may be "explained" – and thereby justified under Article III – "by factors or circumstances unrelated to the foreign origin of the product." Appellate Body Report, *Dominican Republic – Measures Affecting the Importation and Internal Sale of Cigarettes*, WT/DS302/AB/R, adopted 19 May 2005, at para. 96. To recall, the Appellate Body here was expanding on a line of reasoning it started in *Chile - Alcohol* and *Korea – Beef* in which it found that "[a] formal difference in treatment between imported and like domestic products is…neither necessary, nor sufficient, to show a violation of Article III:4. [Rather, the question is] whether a measure modifies the conditions of competition…to the detriment of imported products," at para. 137.

[12] Appellate Body Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products ("U.S. – Shrimp (AB)")*, WT/DS58/AB/R, 12 October 1998, paras. 118-119 (citing *US—Gasoline* case).

[13] In Appellate Body Report, *Brazil – Measures Affecting Imports of Retreaded Tyres* ("*Brazil – Tyres*"), WT/DS332/AB/R, December 3, 2007 (not yet adopted), at paras. 150-1, 172.

A. Does an Exception in GATT Article XX Apply?

1. Article XX(g)

Article XX(g) provides an exception for "measures . . . relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption." The United States has already successfully argued in WTO dispute settlement that U.S. import restrictions on shrimp, which are tied to domestic restrictions on shrimp harvesting designed to protect sea turtles, are justified under Article XX(g). Article XX(g) would be the logical focus for justifying any trade measures on climate change that are otherwise inconsistent with GATT's market access or non-discrimination rules. Under the analysis used in the *US-Shrimp* case, the United States would need to demonstrate that:

- the resources to be protected, *e.g.*, clean air or dry land, are "**exhaustible**,"
- the measures at issue are measures "**relating to**" the conservation of the resource, and
- these measures are "made effective in conjunction with restrictions on domestic production or consumption."

First, in current circumstances, we believe that a WTO dispute settlement panel would agree that clean air and dry land are "exhaustible natural resources" in the sense of Article XX(g). The panel in *U.S. – Gasoline* explicitly found that clean air is a resource that is natural and capable of depletion, even if it is renewable.[14] Later, in *U.S. – Shrimp*, the Appellate Body stated "[w]e do not believe that 'exhaustible' natural resources and 'renewable' natural resources are mutually exclusive."[15] It also found that paragraph (g) must be "read … in the light of contemporary concerns of the community of nations about the protection …of the environment."[16] At present, no concern about the protection of the environment is more important and uniting than the need to reduce GHG emissions, and the fact that the Convention on Climate Change was ratified by all but four UN Members States bears witness to that.[17]

Next, to be a measure "relating to" conservation, the allowance requirement must be crafted to bear a relationship with its stated goals, and must be designed to achieve those goals. Indeed, the Appellate Body has interpreted the phrase "relating to" to mean "primarily aimed at",[18] or evidencing a means and ends relationship.[19] In *U.S. – Gasoline*, the Appellate Body found that the measure at issue permitted "scrutiny and monitoring" of compliance with its environmental objectives. It therefore concluded that the measure, although inconsistent with national treatment, was truly designed to achieve clean air conservation and thus fell within the exception.[20] Likewise, in *U.S. – Shrimp*, the Appellate

[14] Panel Report, *US – Gasoline*, at para. 6.37.
[15] *US – Shrimp (AB)*, at para. 128.
[16] *Id*., para. 129.
[17] See Status of Ratification, available at http://unfccc.int/files/essential_background/convention/status_of_ratification/application/pdf/unfccc_ratification_22.11.06.pdf, last visited April 23, 2007.
[18] Appellate Body Report, *US- Gasoline*, WT/DS2/AB/R, 29 April 1996, p. 16, 18-19.
[19] *US – Shrimp (AB)*, at para. 141.
[20] *US – Gasoline (AB)*, p. 19.

Body focused on the "design and structure" of the measure at issue and was satisfied to find that the measure was narrow enough in scope that it did not constitute a "simple, blanket prohibition" against importation. Consequently, the measure bore a "close and real relationship" with its stated objectives.[21]

In contrast, in *US – Tuna I*,[22] the GATT 1947 Panel noted (in an unadopted report) that because the United States had "linked the maximum incidental dolphin-taking rate which Mexico had to meet during a particular period in order to be able to export tuna to the United States to the taking rate actually recorded for United States fisherman during the same period," the "Mexican authorities could not know whether, at a given point of time, their conservation policies conformed to the United States conservation standards."[23] The Panel concluded that "a limitation on trade based on such unpredictable conditions could not be regarded as being primarily aimed at the conservation of dolphins."[24]

Finally, to show that the allowance requirement program is "made effective in conjunction with restrictions on domestic production or consumption," the U.S. would have to show that if and where a requirement for allowances burdens imports, these allowances also burden domestic goods.[25] This test requires only "even-handedness,"[26] not "equality of treatment."[27] If a measure did not accord less favorable treatment to imports than it did domestic goods, it would not offend Article III, and therefore, would not need to be justified under an exception. On the other hand, a measure that solely burdens imports is not likely to be considered as even-handed, and would not find shelter under paragraph (g).[28] The import component of the allowances program is not intended to impose on foreign producers all or a disproportionate amount of the program's costs—it is intended to achieve appropriate burden-sharing in the shared fight against global warming, ideally through measures negotiated and adopted by governments. And even-handedness, because of the balance it strikes, sets a standard that the United States can meet in crafting climate change legislation.

An emissions allowances requirement falls within the policy-based exception for conservation in Article XX(g). As discussed above, the United States should encounter no difficulty arguing that clean air or dry land or other environmental resources put at risk by climate change are exhaustible natural resources threatened with depletion by GHG emissions. As for the second element under Article XX(g), "relating to," the Appellate Body has interpreted it in the *U.S. – Gasoline* and *U.S. – Shrimp* cases in a way that leads us to conclude that the United States could satisfy the standard it sets—since the allowances requirement is designed to effectively limit emissions by requiring presentation of allowance certificates.

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[21] *US – Shrimp (AB)*, at para.141.
[22] Panel Report, *United States – Restrictions on Imports of Tuna (Tuna I)*, DS21/R, GATT BISD 39S/155 (circulated 3 September 1991; not adopted).
[23] *Tuna I*, at para.5.28.
[24] *I.d*
[25] For example, in *U.S. – Shrimp*, the United States required shrimp trawlers to use turtle excluder devices (TED) to exclude turtles from their nets when fishing in waters that are likely to be turtle habitat. Exporting countries had to demonstrate their use of TEDs in order to be certified to export to the United States. Domestically, the United States required that shrimp trawlers use TEDs and imposed civil and criminal penalties (later changed to civil penalties and monetary sanctions) on offenders. See *U.S. – Shrimp (AB)*, at para. 144.
[26] *U.S. – Gasoline (AB)*, p. 20-21; *US-Shrimp (AB)*, at paras. 144-45.
[27] *U.S. – Gasoline (AB)*, p. 21.
[28] *U.S. – Gasoline (AB)*, p. 21.

Lastly, the United States could meet the requirement of even-handedness by applying the allowances requirement to domestic industry and enforcing the domestic program to compel producer reporting and compliance with the emissions caps. No WTO panel will accept a U.S. GHG reduction program that shifts all or a disproportionate part of the burden of GHG reduction to foreign producers, by restricting imports while giving a break to domestic producers. Even-handedness also rules out free rides—the United States must exempt from the allowances requirement all those countries that have adopted meaningful and satisfactory (i.e., comparable) emission reductions. On the other hand, the United States could exempt from coverage countries whose GHG emissions are below some *de minimis* level, as imposition of the allowance requirement to goods of such countries would not contribute to the non-trade policy objective of the program.

2. Article XX(b)

Article XX(b) offers an additional defense. It provides an exception for measures that are "necessary to protect human, animal or plant life or health." The United States would need to demonstrate:

- that the *policy* in respect of the measures for which the provision was invoked fell within the range of policies designed to protect human, animal or plant life or health; and

- that the inconsistent measures for which the exception was being invoked were *necessary* to fulfill the policy objective.[29]

First, we believe that a WTO dispute settlement panel would agree that a measure designed to curb climate vulnerability and its resulting effect on the spread and increased susceptibility of populations to disease and death would be a measure to protect human, animal and plant life or health within the meaning of Article XX(b). The World Health Organization has made a number of explicit findings linking climate change to significant public health problems that support this conclusion.[30] The Panel in *U.S. – Gasoline* found that Clean Air Act gasoline standards were designed to protect health and life.[31] Similarly, in *Brazil – Tyres* the Appellate Body found that Article XX(b) is satisfied by a measure to ban the importation of used tires because the accumulation of used tires contributed to the spread of disease and toxic tire fires.[32]

Second, in order to demonstrate that a trade-restrictive measure is "necessary" a country must show ""that the measure is apt to make a material contribution to the achievement of its objective."[33] To this end, the Appellate Body has recognized that "certain complex public health or environmental problems may be tackled only with a comprehensive policy comprising a multiplicity of interacting measures."[34] As an example of the type of objective that may require a longer time frame to demonstrate a contribution, the Appellate Body noted that "for instance, measures adopted in order to attenuate global warming and

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[29] Panel Report, *US – Gasoline*, at para. 6.20.
[30] *See, e.g.,* Bulletin of the World Health Organization, *Global Climate Change: Implications for International Public Health Policy* (March 2007), available at: http://www.who.int/bulletin/volumes/85/3/06-039503/en/index.html, last visited January 25, 2008.
[31] Panel Report, *US – Gasoline*, at para. 6.21.
[32] Appellate Body Report, *Brazil – Tyres*, at para. 136.
[33] Appellate Body Report, *Brazil – Tyres*, at para. 150.
[34] Appellate Body Report, *Brazil – Tyres*, at para. 151.

climate change, or certain preventive actions to reduce the incidence of diseases that may manifest themselves only after a certain period of time—can only be evaluated with the benefit of time."

Additionally, where the measure at issue is part of a comprehensive policy , the Appellate Body has noted that "[s]ubstituting one element of this comprehensive policy for another would weaken the policy by reducing the synergies between its components, as well as its total effect."[35]

An emissions allowance requirement for imports meets these criteria because it is part of a comprehensive policy that has synergies between its components and because it is apt to materially contribute to the reduction of carbon emissions, even if proof of that fact requires the benefit of time to demonstrate.

B. Does the Measure Satisfy the GATT's Safeguards Against Abuse?

As discussed above, all of the GATT's policy-based exceptions are subject to two safeguards provided in a general opening clause ("*chapeau*") to Article XX. This clause provides that measures that fall within the policy-based exceptions in Article XX may not be **applied in a manner** which would constitute **arbitrary or unjustifiable discrimination** between countries where the same conditions prevail, or a **disguised restriction on international trade**. The issue here is not the substance of a measure, but how it is applied. A WTO panel or the Appellate Body may agree entirely that a measure is a legitimate use of Article XX, but at the same time find that the way this legitimate measure is applied constitutes arbitrary or unjustified discrimination or disguised protectionism.

"Arbitrary or unjustifiable discrimination" in this context is discrimination not between products, but between countries where the same conditions prevail. The discrimination in question can be discrimination between the United States and one or more foreign countries, or it can be discrimination between different foreign countries. Different treatment of countries is permissible and even appropriate where these countries have objectively different conditions.[36] In practice, this proviso has been interpreted to bar an importing country from using an economic embargo to require its trading partners to adopt "essentially the same comprehensive regulatory program, to achieve a certain policy goal, as that in force within the Member's own territory, *without* taking into account different conditions which may occur in the territories of those other Members."[37] By requiring that the decision on "comparable action" take into account the extent to which a country has deployed state-of-the-art technologies, and implemented other conservation techniques or actions, the IBEW-AEP proposal would meet this requirement under the *chapeau*.

The ban on arbitrary discrimination has also been interpreted to require that advantages offered to one trading partner must be equally available to other similarly

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[35] Appellate Body Report, *Brazil – Tyres*, at para. 172.

[36] For example, in *Brazil – Tyres*, Brazil initially applied an import ban on tires from all origins, but then provided an exemption for tires from MERCOSUR countries. The panel found that the exemption constituted discrimination, but that the discrimination "[did] not seem to be motivated by capricious or unpredictable reasons." It found rather that the discrimination was due "to a ruling within the MERCOSUR framework [with] binding legal effects for Brazil." Panel Report, *Brazil – Tyres*, at para. 7.272. More importantly, the panel found that notwithstanding the ban, retreaded tires from non-MERCOSUR countries were still entering Brazil along with tires from MERCOSUR countries. The panel thus concluded that the discrimination resulting from the ban was arbitrary or unjustifiable under Article XX. Panel Report, *Brazil – Tyres*, at para. 7.306.

[37] *U.S. – Shrimp (AB)*, at para. 163-164; see also para. 177.

situated trading partners. For instance, in the *US—Shrimp* case, the United States adopted a cooperative approach and negotiated an agreement on sea turtle protection with Caribbean nations, but did not pursue any negotiations with other WTO Members, including nations of the Western Pacific. The Appellate Body found that to avoid arbitrary or unjustifiable discrimination, the United States had to provide all exporting countries similar opportunities to negotiate an international agreement, by engaging in "serious, across-the board negotiations with the objective of concluding bilateral or multilateral agreements" on sea-turtle protection.[38] Nevertheless, although the United States had to make good faith efforts to reach agreements that are comparable from one forum of negotiation to another, its failure to reach comparable agreements did not constitute arbitrary or unjustifiable discrimination.[39]

Additionally, the discrimination must be evaluated based on its rationale rather than its effect.[40] That is, discrimination must have a rational connection to the objective of the measure, as described in one of the separate paragraphs of Article XX.[41]

The transparency and predictability of a measure are also relevant. In the *U.S. – Shrimp* case, the Appellate Body found the "informal" and "casual" nature of the certification process deprived it of basic fairness and due process, tarnished its transparency and predictability, and therefore, rendered it discriminatory in an arbitrary and unjustifiable manner.[42]

The requirement that the measure not constitute a "disguised restriction on international trade" has been defined as including restrictions that are actually discriminatory but are taken under guise of a legitimate Article XX exception: in effect, a form of stealth protectionism.[43]

As proposed by IBEW-AEP, U.S. climate change legislation would treat imports of products of countries that have *not* taken comparable action on GHG emissions less favorably than imports from a country that have done so. This difference in treatment would be justified under Article XX(g) of the GATT, for the reasons (and under the circumstances) described above. But in that case, the ban on arbitrary discrimination in the opening clause (*chapeau)* of Article XX would require that, if the United States were to negotiate with some countries before imposing the measure, it undertake "serious, across-the board negotiations with the objective of concluding bilateral or multilateral agreements" on GHG reduction, with *all* concerned parties. The United States would not have to reach agreements with these other countries, but it would have to make a non-discriminatory, good faith effort with each one. Second, the United States would have to take its trading partners' differences in circumstances into account in devising and implementing its measures. Finally, the U.S. measures would have to be implemented with due process and fairness. The IBEW-AEP proposal for U.S. climate change legislation meets these standards.

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[38] *U.S. – Shrimp (AB)*, para. 166.
[39] *U.S. – Shrimp (AB)*, para. 166; Appellate Body Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products: Recourse to Article 21.5 of the DSU by Malaysia ("US – Shrimp (21.5 AB)*, WT/DS58/AB/RW, 22 October 2001, at paras. 122-134.
[40] Appellate Body Report, *Brazil – Tyres*, at para. 229.
[41] Appellate Body Report, *Brazil – Tyres*, at para. 227.
[42] *U.S. – Shrimp (AB)*, at paras. 180-81.
[43] *U.S. – Gasoline (AB)*, p. 25.

As we have discussed, the United States would appear to be in a strong position to defend a requirement that importers of goods from a country must present emission allowance certificates to cover the GHG emissions represented by the goods. First, such a measure is clearly linked to the purpose of GHG emissions reduction. Second, this would be a flexible measure adaptable to the circumstances of each exporting country, and therefore devoid of arbitrary or unjustifiable discrimination. Each exporting country would have a choice to implement any GHG emission reduction program as an alternative to forcing importers into presenting allowance certificates, and trading partners would be given a predictable standard in advance with which to achieve compliance. Third, the design, architecture, and structure of such an allowances requirement would demonstrate that the system has no purpose other than to cause the reduction of GHG emissions. Consequently, the *chapeau* of Article XX would pose no obstacle to deployment of a U.S. allowances program to combat climate change.

Attachment

APPENDIX OF RELEVANT WTO PROVISIONS

1. GATT Article I: General Most-Favored-Nation Treatment

1. With respect to customs duties and charges of any kind imposed on or in connection with importation or exportation…any advantage, favour, privilege or immunity granted by any [Member] to any product originating in or destined for any other country shall be accorded immediately and unconditionally to the like product originating in or destined for the territories of all other [Members].

2. GATT Article II: Schedules of Concessions

1. (a) Each [Member] shall accord to the commerce of the other [Member] treatment no less favorable than that provided for in the appropriate Part of the appropriate Schedule.

(b) The products described in Part I of the Schedule…shall, on their importation into the territory to which the Schedule relates…be exempt from ordinary customs duties in excess of those set forth and provided therein. Such products shall also be exempt from all other duties or charges of any kind imposed on or in connection with the importation in excess of those imposed thereafter by legislation in force in the importing territory on that date.

3. GATT Article III: National Treatment on Internal Taxation and Regulation

1. The [Members] recognize that internal taxes and other internal charges, and laws, regulations and requirements affecting the internal sale, offering for sale, purchase, transportation, distribution or use of products, . . . should not be applied to imported or domestic products so as to afford protection to domestic production.

2. The products of the territory of any [Member] imported into the territory of any other [Member] shall not be subject, directly or indirectly, to internal taxes or other internal charges of any kind in excess of those applied, directly or indirectly, to like domestic products. . . .

4. The products of the territory of any [Member] imported into the territory of any other [Member] shall be accorded treatment no less favourable than that accorded to like products of national origin in respect of all laws, regulations and requirements affecting their internal sale, offering for sale, purchase, transportation, distribution or use. . . .

4. GATT Note Ad Article III

Any internal tax or other internal charge, or any law, regulation or requirement of the kind referred to in paragraph 1 which applies to an imported product and to the like domestic product and is collected or enforced in the case of the imported product at the time or point of importation, is nevertheless to be regarded as an internal tax of other internal charge, or a law, regulation or requirement of the kind referred to in paragraph 1, and is accordingly subject to the provisions of Article III.

5. GATT Article XI: General Elimination of Quantitative Restrictions

1. No prohibitions or restrictions other than duties, taxes or other charges, whether made effective through quotas, import or export licences or other measures, shall be instituted or maintained by any [Member] on the importation of any product of the territory of any other [Member] or on the exportation or sale for export of any product destined for the territory of any other [Member].

6. GATT Article XIII: Non-Discriminatory Administration of Quantitative Restrictions

1. No prohibition or restriction shall be applied by any [Member] on the importation of any product of the territory of any other [Member] or on the exportation of any product destined for the territory of any other [Member], unless the importation of the like product of all third countries or the exportation of the like product to all third countries is similarly prohibited or restricted.

7. GATT Article XX: General Exceptions

Subject to the requirement that such measures are not applied in a manner which would constitute a means of arbitrary or unjustifiable discrimination between countries where the same conditions prevail, or a disguised restriction on international trade, nothing in this Agreement shall be construed to prevent the adoption or enforcement by any [Member] of measures:

* * *

(b) necessary to protect human, animal or plant life or health;

* * *

(g) relating to the conservation of exhaustible natural resources if such measures are made effective in conjunction with restrictions on domestic production or consumption.

The IBEW – AEP International Proposal –
How it Operates within Climate Change Legislation

1. What are the objectives?

   - The goal is to establish an environmental framework in the context of U.S. mandatory greenhouse gas (GHG) emissions reductions, using the leverage of the U.S. marketplace.

   - The framework seeks to –

     - strengthen the hand of negotiators seeking to reach a global solution to the global climate change problem,

     - induce large emitting countries to take action and achieve meaningful results, and by doing so also:

     - prevent the shifting of U.S. jobs to countries that would have lower manufacturing costs merely because they refuse do their part to limit greenhouse gas (GHG) emissions.

2. Which countries are covered?

   - The allowance requirement only applies to foreign countries that are –

     - large-emitters of GHG emissions, and

     - not taking "comparable action" to address their emissions.

   - Foreign countries are excluded if they –

     - have taken "comparable action" to limit their GHG emission;

     - are among the poorest developing countries, or

     - have de minimis levels of GHG emissions.

3. How is "comparability" determined?"

   - First, action is deemed "comparable" if

     - percentage change in GHG emissions in the foreign country is equal to or higher than

     - percentage change in the U.S. in the relevant period.

   - If the foreign country fails the first test, then new US Commission still may deem action "comparable" taking into account the extent of –

     - Deployment and use of state-of-the-art technologies, and

- Implementation of regulatory programs.

4. When does the allowance requirement apply?

   - To fully comply with WTO, the U.S. first must make good faith efforts to negotiate with foreign countries affected by the program to limit their GHG emissions.
     - WTO requires that, if U.S. negotiates with some countries, must negotiate with all countries affected by program.
   - The allowance requirement is a measure of last resort that applies after the promulgation of regulations and the state of the U.S. cap-and-trade program.

5. How does the allowance requirement work?

   - U.S. importers must hold allowances (see below) to cover emissions from imported goods.
   - Failure to submit allowances bars entry of imported goods into the U.S.
   - The allowance requirement –
     - applies after the start of the U.S. cap-and-trade program, and
     - strives to mirror allowance requirement that the U.S. program imposes on producers of domestic goods, and
     - the comparability and allowance determination, as with other key decisions, is made by an independent and bipartisan commission.

6. How do importers comply?

   - Importers may comply with the allowance requirement by –
     - obtaining emission allowances issued pursuant to other foreign GHG regulatory programs
     - obtaining certified emissions credits issued pursuant to the U.S. program or other foreign GHG regulatory programs
     - purchasing "international reserve allowances" from a separate pool that is reserved only for this purpose (see below)

7. What are the key features of international reserve allowances?

   - The allocation of international reserve allowances will not reduce the number of allowances allocated for domestic compliance.
   - The international reserve allowances –
     - cannot be used for domestic compliance, and

- can only be used for meeting the allowance requirement applicable to imported covered goods.

- The price of the international reserve allowances would be pegged at the U.S. market price for domestic allowances.

- International reserve allowances may be traded and banked for future use.

8. Which goods are covered?

- The allowance requirement applies initially to "greenhouse gas intensive" goods from countries that are found not to have taken action comparable to the U.S.

- Covered goods include –

  - primary goods (such as iron and steel, aluminum, cement, bulk glass, and paper) and

  - manufactured goods for consumption that generate a substantial quantity of direct and indirect GHG emissions.

- Limiting the primary scope of the program addresses concerns that the international allowance provision will interfere with international trade with respect to the vast amount of imported goods that do not generate significant GHG emissions during their manufacture.

9. How is the allowance requirement set?

- The allowance requirement is –

  - set for each category of covered goods from each covered foreign country,

  - applied on a per unit basis to each good,

  - adjusted each year to reflect production changes in the foreign country,

  - adjusted to ensure consistency with WTO requirements.

10. What adjustments do WTO rules require?

- To ensure WTO compliance, adjustments are made to each category of covered goods.

- The WTO adjustments are intended to –

  - avoid discrimination between countries where the same conditions prevail.

  - Example: Take into account the extent to which state-of-the-art technologies and regulatory programs are deployed.

  - maintain rough comparability in burden on imported and domestic goods.

11. Can the allowance requirement be adjusted further?

- The Commission can increase the stringency of the international allowance requirement or take other appropriate action to address GHG impacts of imports.
- Either action is authorized if –
    - the Commission determines the current requirement is insufficient to address GHG impacts, and
    - the adjusted requirement complies with WTO laws.
- The Administrator also may make adjustments to ensure other aspects of implementation of the program are WTO compliant.